

SUBCOMMITTEE VII  
THE NEED FOR CHANGES IN THE TAX LAWS AS A  
MEANS FOR PRESERVING AGRICULTURAL LAND  
Senator James Clark, Jr., Chairman

Some sources say that land in farming has declined at the rate of about 60,000 acres annually over the last 20 years. This decline in farm acreage has caused considerable concern among both farm and non-farm groups. This concern has been expressed by many of the citizens of Maryland as well as those in other states. It is the purpose of this paper to look at tax legislation and its effect on this problem.

I. Past Legislation re: Taxes

During the 1950's, evidence seemed to indicate that farmland, particularly farmland near urbanized areas, was being "financially pushed" into other uses because it was taxed according to valuations based on its non-farm use. In 1956, a law was enacted in Maryland to require the assessment of farmland for property tax purposes according to its "use-value" in farming as opposed to any other basis. It was generally believed that among other effects, this law would retard the rate of exit of farmland from farming to other uses. While the Maryland Farmland Assessment Law has slowed the conversion of farmland to other use, it has not prevented it. Furthermore, Federal Estate taxes and State Inheritance tax laws which have not been changed since 1942 often force the conversion of farmland to non-farm uses.

II. Current Tax Laws

The taxes on intergeneration transfer of wealth include death taxes (Federal Estate tax and State Inheritance tax) and gift taxes.

#### A. Estate Taxes

These are taxes levied by the Federal Government and a number of states. They include levies on the entire estate left by a decedent. The Federal Government's estate tax became a permanent part of the Federal revenue system in 1916. At that time the Federal tax included a \$50,000 exemption and taxation rates from 1% to 10%. The current law, established in 1941-42, provides for a \$60,000 exemption with marginal rates of taxation varying from 3% to 77%.

#### B. Gift Taxes

These were introduced into the Federal laws in 1932 and include nominal rates equal to 3/4 of the Federal estate taxes. This gift tax structure (rates and exemptions) has not changed since 1942.

Federal estate and gift taxes have provided about 2% of the total Federal tax receipts over the last five years.

#### C. Inheritance Taxes

Inheritance taxes are levied on separate shares of an estate which are transferred to beneficiaries. Thus, inheritance taxes may be thought of as a tax on the privilege to receive property by an heir. Frequently, the tax rates on shares passed to close relatives are less than the tax rates on those shares passed on to others. (It should be noted that inheritance taxes are state taxes, while estate taxes are levied by the Federal Government.)

#### D. Taxation Rates

The Federal estate tax rate schedules are shown in Appendix I. The amount

of tax is determined by applying the estate tax rates to the taxable estate.

The taxable estate is determined by subtracting deductible allowances from the gross estate value. The gross estate value is determined as follows: it is the total value of property transferred at time of death plus the value of property transferred by gift within the last three years, if such gifts were made in contemplation of death. \*

The value of property is determined as follows: Assign the market prices to quantities of physical property transferred at time of death. When items transferred are not sold, the value of the property is obtained from similar types of property which were sold.

Deductible allowances from the gross estate value include the following:

1. The debts of the decedent
2. Funeral expenses
3. Administrative expenses
4. Exemptions
5. Property passing to a surviving spouse not to exceed 50% of the gross estate value minus deductions for debts of the decedent, funeral, and estate administrative expenses.

\*All property transferred by gift three years before the time of death is presumed to have been in contemplation of death unless the estate can prove otherwise.

### III. The Estate Tax Problem As It Pertains To Agricultural Land

Under the present system of taxation, a decedent's farmland estate is assessed at its fair market value rather than at its being assessed for its value in agriculture. This has resulted in the heir(s) having few liquid assets with which to pay the estate taxes. The heir is often forced to sell a portion of the land in order to pay the estate taxes. This sale is often made to developers in lieu of other farmers.

### IV. A Proposed Solution To The Problem

This proposal is based on the deferred tax concept. It would provide the necessary relief to those families faced with a substantial estate tax burden. This proposal is advantageous in that it does not deny the Federal Government any of its estate tax revenue.

Any estate containing land currently used for farming and being passed by a will or by laws of intestacy to another member of the family who will continue to farm it will be assessed on the following two bases:

1. The highest value and best use for land similarly situated in the surrounding area, and
2. The value of the land as farmland.

At the time the estate is settled, the estate would be liable only for the payment of inheritance taxes based on the value under 2 above. The difference in taxes, if any, between its value as farmland and its assessed value when it is to be used for other purposes would not become due at the time the estate was closed. Instead, it would become a lien upon the land which would remain uncollected as long as the land continued in farming.

At such time as the land were sold or otherwise converted to non-farm use, the lien would have to be satisfied and the difference in taxes at the time of sale would be paid.

#### V. Benefits of Such A Solution

1. This solution would have the effect of encouraging the continued use of the land in farming while, at the same time, deferring what would presumably be a higher tax burden until such time as the owner would have the cash to pay the taxes.
2. There is precedence for such an approach under current income tax statutes to homeowners. Homeowners, upon sale of their personal residence and realization of a profit, may defer payment of income tax based on that gain if, within a year's time, they purchase another personal residence at a cost equal to or greater than the sale price of their previous residence.
3. There is the desirable effect of offering a legislative solution which does not require the government to forgive any taxes to which it is otherwise entitled under the Federal Inheritance Tax Laws. A suitable definition of "farming" is needed to satisfy the legislators that this legislation could not be used for any purpose except to encourage the continuance of legitimate farming operations.
4. The true problem is restricted to that situation in which farmland is being passed to a member of the family of the testator. The proposed solution would not extend beyond this situation.

In other words, if a farm owner dies, passes his farm estate to a member of the family who does not desire to continue farming, but would sell the land, it could be assumed that the sale would be based not on the value of

the land as farmland (whether or not it were being sold for that purpose) but rather on the best use and highest value of the land with a corresponding price. Therefore, the problem of the effect of the inheritance tax would not exist in such a case. The estate would have sufficient funds at that time to meet the tax burden created by the value of the property when assessed for other than farm purposes.

An example of this proposal using an actual case as a source of data can be seen in Appendix II. These two computations were done (a) using the present system whereby the land is taxed based on its fair market value, and (b) using the aforementioned proposal whereby land is assessed on the basis of its agricultural value. Note that the net estate tax payable under current tax laws is \$96,174.91. If the estate tax were based on agricultural use value, the tax would equal \$37,239.05--a tax deferment of \$59,035.86. This deferment would obviously be an incentive to keep the land in agriculture.

Table 1

Taxable estate <sup>1</sup> equal to or more than— <sup>2</sup> (A)	Taxable estate <sup>1</sup> less than— <sup>2</sup> (B)	Tax on amount in column (A) (C)	Rate of tax on excess over amount in column (A) (D)
Percent			
0	\$5,000	0	3
\$5,000	10,000	\$150	7
10,000	20,000	500	11
20,000	30,000	1,600	14
30,000	40,000	3,000	18
40,000	50,000	4,800	22
50,000	60,000	7,000	25
60,000	100,000	9,500	28
100,000	250,000	20,700	30
250,000	500,000	65,700	32
500,000	750,000	145,700	35
750,000	1,000,000	233,200	37
1,000,000	1,250,000	325,600	39
1,250,000	1,500,000	423,200	42
1,500,000	2,000,000	528,200	45
2,000,000	2,500,000	753,200	49
2,500,000	3,000,000	998,200	53
3,000,000	3,500,000	1,263,200	56
3,500,000	4,000,000	1,543,200	59
4,000,000	5,000,000	1,838,200	63
5,000,000	6,000,000	2,468,200	67
6,000,000	7,000,000	3,138,200	70
7,000,000	8,000,000	3,838,200	73
8,000,000	10,000,000	4,568,200	76
10,000,000		6,088,200	77

Table 2—Federal gift tax rate schedule, 1942 to date

Amount of taxable gifts <sup>1</sup> equaling— (A)	Amount of taxable gifts <sup>1</sup> exceeding— (B)	Tax on amount in column (A) (C)	Rate of tax on excess over amount in column (A) (D)
Percent			
0	\$5,000	\$112	2-1/4
\$5,000	10,000	375	5-1/4
10,000	20,000	1,200	8-1/4
20,000	30,000	2,250	10-1/4
30,000	40,000	3,600	13-1/4
40,000	50,000	5,250	16-1/4
50,000	60,000	7,125	18-1/4
60,000	100,000	15,525	21
100,000	250,000	49,275	22-1/4
250,000	500,000	49,275	24
500,000	750,000	109,275	26-1/4
750,000	1,000,000	174,900	27-1/4
1,000,000	1,250,000	244,275	29-1/4
1,250,000	1,500,000	317,400	31-1/4
1,500,000	2,000,000	396,150	33-1/4
2,000,000	2,500,000	564,900	36-1/4
2,500,000	3,000,000	748,650	39-1/4
3,000,000	3,500,000	947,400	42
3,500,000	4,000,000	1,157,400	44-1/4
4,000,000	5,000,000	1,373,650	47-1/4
5,000,000	6,000,000	1,851,150	50-1/4
6,000,000	7,000,000	2,352,650	52-1/4
7,000,000	8,000,000	2,878,650	54-1/4
8,000,000	10,000,000	3,425,150	57
10,000,000	—	4,566,150	57-1/4

Table 3—Tax cost of transferring various amounts under Federal  
estate versus Federal gift tax

APPENDIX I(cont)

Net amount trans- ferred through estate or gift after tax is paid	Gift tax		Estate tax		Gift tax as a percentage of estate tax
	Amount	Percent <sup>1</sup>	Amount	Percent <sup>1</sup>	
\$4,850	\$109.13	2.3	\$150	3.1	72.8
9,500	348.75	3.7	500	5.3	69.8
18,400	1,068.00	5.8	1,600	8.7	66.8
27,000	1,935.00	7.2	3,000	11.1	64.5
35,200	2,952.00	8.4	4,300	13.6	61.5
43,000	4,095.00	9.5	7,000	16.3	58.5
50,500	5,343.75	10.6	9,500	18.8	56.2
70,300	11,178.00	14.1	20,700	26.1	54.0
184,300	34,492.50	18.7	65,700	35.6	52.5
354,300	74,307.00	21.0	145,700	41.1	51.0
516,800	113,685.00	22.0	233,200	45.1	48.8
675,300	155,291.25	23.0	325,700	48.2	47.7
826,800	196,212.00	23.7	423,200	51.2	46.4
971,800	236,449.50	24.3	528,200	54.4	44.8
1,246,200	316,464.00	25.4	753,200	60.4	42.0
1,501,800	396,757.50	26.4	998,200	66.5	39.7
1,737,800	476,407.50	27.4	1,263,200	72.7	37.7
1,957,800	550,657.50	28.1	1,543,200	78.8	35.7
2,161,800	624,361.50	28.9	1,838,200	85.0	34.0
2,531,800	761,290.50	30.1	2,468,200	97.5	30.8
3,911,800	1,339,621.50	34.2	6,088,200	155.6	22.0
10,000,000	4,566,150.00	45.7	26,470,435	264.7	17.2

<sup>1</sup>Percent of net amount transferred, not the tax rate.



*fair market*  
ESTATE TAX USING LAND VALUE OF \$1296.00/ACRE

(1) and attach a certified copy of the will.

Computation of Tax

Has a prior estate tax return been filed, have any prior estate tax payments been made, or have certain marketable United States Treasury bonds been redeemed as explained in General Instruction E in the separate instructions? ☐ Yes ☒ No  
If "Yes," attach explanation.

Part I	1 Total gross estate (from Recapitulation, page 3)	440,465.27
	2 Total allowable deductions (from Recapitulation, page 3)	10,691.27
	3 Exemption	60,000.00
	4 Total deductions plus exemption	70,691.27
	5 Taxable estate (item 1 minus item 4)	369,774.00
Part II	6 Gross estate tax (use Table A in separate instructions)	104,027.68
	7 Credit for State death taxes (use Table B in separate instructions and furnish credit evidence)	7,752.77
	8 Gross estate tax less credit for State death taxes (item 6 minus item 7). This is the net amount payable unless credit for Federal gift taxes, foreign death taxes, or tax on prior transfers is claimed in Part III.	96,274.91
Part III	9 Credit for Federal gift taxes (Attach computation.)	
	10 Credit for foreign death taxes (from Schedule O) (Form 706CE is required.)	
	11 Credit for tax on prior transfers (from Schedule P)	
	12 Total of credits under Part III (total of items 9, 10, and 11)	
	13 Net estate tax payable (item 8 minus item 12)	96,274.91

Please attach the necessary supplemental documents; see General Instruction F in the separate instructions.

Under penalty of perjury, I declare that this return, including accompanying statements, has been examined by me, and is, to the best of my knowledge and belief, true, correct, and

*agricultural*  
ESTATE TAX USING LAND VALUE OF \$300.00/ACRE

Computation of Tax

Has a prior estate tax return been filed, have any prior estate tax payments been made, or have certain marketable United States Treasury bonds been redeemed as explained in General Instruction E in the separate instructions? ☐ Yes ☒ No  
If "Yes," attach explanation.

1 Total gross estate (from Recapitulation, page 3)	233,463.27
2 Total allowable deductions (from Recapitulation, page 3)	10,691.27
3 Exemption	60,000.00
4 Total deductions plus exemption	70,691.27
5 Taxable estate (item 1 minus item 4)	162,772.00
6 Gross estate tax (use Table A in separate instructions)	38,985.62
7 Credit for State death taxes (use Table B in separate instructions and furnish credit evidence)	-1746.57
8 Gross estate tax less credit for State death taxes (item 6 minus item 7). This is the net amount payable unless credit for Federal gift taxes, foreign death taxes, or tax on prior transfers is claimed in Part III.	37,239.05
9 Credit for Federal gift taxes (Attach computation.)	
10 Credit for foreign death taxes (from Schedule O) (Form 706CE is required.)	
11 Credit for tax on prior transfers (from Schedule P)	
12 Total of credits under Part III (total of items 9, 10, and 11)	
13 Net estate tax payable (item 8 minus item 12)	37,239.05

Please attach the necessary supplemental documents; see General Instruction F in the separate instructions.